Nos. 84-550 and 84-867

In the Supreme Court of the United States

OCTOBER TERM, 1984

INTERSTATE COMMERCE COMMISSION, PETITIONER

v.

BRAE CORPORATION, ET AL.

CONSOLIDATED RAIL CORPORATION, PETITIONER

v.

AHNAPEE & WESTERN RAILWAY COMPANY, ET AL.

ON PETITIONS FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE UNITED STATES

REX E. LEE
Solicitor General

J. PAUL MCGRATH
Assistant Attorney General

LOUIS F. CLAIBORNE
Deputy Solicitor General

MICHAEL W. MCCONNELL
Assistant to the Solicitor General

JOHN J. POWERS, III
JOHN P. FONTE
Attorneys

Department of Justice
Washington, D.C. 20530
(202) 633-2217

QUESTIONS PRESENTED

1. Whether, in determining to exempt railway boxcar traffic from regulations regarding joint rates among connecting railroad lines, the Interstate Commerce Commission was required to ensure that the proposed exemption would preserve the court's conception of a "fair division" of revenues among carriers participating in joint rate agreements, a requirement not contained in the statutory exemption provision or the National Rail Transportation Policy.

2. Whether a partial exemption from certain regulations regarding the interchange of boxcars among railroads, which would have the effect of introducing market incentives into an otherwise-regulated relationship, constitutes "regulation" rather than "deregulation" and is thus beyond the scope of the Commission's exemption authority.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-93a) is reported at 740 F.2d 1023. The initial decision of the Interstate Commerce Commission (Pet. App. 103a-152a) is reported at 367 I.C.C. 423, and its opinion on denial of motions for reconsideration (Pet. App. 153a-189a) is reported at 367 I.C.C. 745. The Commission's denial of motions for a stay pending judicial review (Pet. App. 190a-214a) is not reported.

JURISDICTION

The judgment of the court of appeals (Pet. App. 219a-220a) was entered on June 27, 1984, and peti-

tions for rehearing were denied on August 27, 1984 (Pet. App. 96a, 97a-98a). The petition for a writ of certiorari in No. 84-550 was filed on October 4, 1984. The petition in No. 84-867 was filed on November 26, 1984. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1) and 2350(a).

STATEMENT

1. Regulatory Framework

In 1976, and again in 1980, Congress passed legislation departing in major respects from the century-old scheme of pervasive regulation of railroads under the Interstate Commerce Act. Among the key features of the traditional scheme was the required publication and filing of tariffs by railroads specifying each of their freight rates, with an opportunity for shippers and competitors to challenge those rates before the Commission either when they were filed or at any time thereafter. Pet. App. 106a; see *Arizona Grocery Co.* v. *Atchison, T. & S.F. Ry.*, 284 U.S. 370 (1932). As the Commission has noted (Pet. App. 106a), this regulatory regime was designed to "preserve rather complex, rigid relationships among the freight rates charged to competing shippers located throughout the country."

A particularly rigid aspect of this scheme was its treatment of "joint rates." A joint rate is a single rate charged by two or more railroads for transportation over interconnecting lines; the joint rate agreement provides for the division of revenues among the participating carriers. Once a railroad entered into a joint rate agreement, it could not withdraw, or change the terms of the tariff, in the absence of consent by other participants, without the threat of suspension of the revised tariff by the Commission and initiation of an adversarial proceeding. As the Commission has noted (Pet. App. 106a), making a change

in a joint rate under this system was "extraordinarily expensive and time consuming." See also *Southern Ry.* v. *ICC*, 681 F.2d 29, 34 (D.C. Cir. 1982).

This complex system of railroad regulation was predicated on the assumption that railroads had extensive market power over the shippers they served. However, with the rise of competitive modes of transportation, especially trucking, railroads lost revenue and often found it difficult to compete, in part because of the rigidities of the regulatory regime. See S. Rep. 96-470, 96th Cong., 1st Sess. 5 (1979). With the bankruptcy of the Penn Central and other railroads in the 1970s, the national railway system was seen to be in crisis, and Congress determined that the decline of the industry was caused in large part by excessive governmental regulation. See, *e.g.*, S. Rep. 94-499, 94th Cong., 1st Sess. 2-4, 10-11 (1975).

Congress's first response, in 1976, was the Railroad Revitalization and Regulatory Reform Act of 1976, 45 U.S.C. 801 *et seq.* Among other deregulatory aspects of that legislation, Congress authorized the Commission to exempt from regulation services or transactions that were of "limited scope" where regulation was found to impose an "undue burden" and to "serve little or no useful public purpose." See 49 U.S.C. (Supp. IV 1980) 10505. The Commission was required to provide notice and an opportunity for a hearing to interested parties before either making an exemption or revoking it. 49 U.S.C. (Supp. IV 1980) 10505(a) and (d).

Congress soon recognized that the reforms of the 1976 Act had not sufficiently improved the ability of the railroads to compete for traffic. See H.R. Conf. Rep. 96-1430, 96th Cong., 2d Sess. 79 (1980). Consequently, it enacted the Staggers Rail Act of 1980, 49 U.S.C. 10101 *et seq.* In Section 2(3) and (9) of

the Act, 49 U.S.C. 10101a note, Congress declared its findings that today "most transportation within the United States is competitive" and that "modernization of economic regulation for the railroad industry with a greater reliance on the marketplace is essential in order to achieve maximum utilization of railroads." As part of the Act, Congress established a 15-element National Rail Transportation Policy, 49 U.S.C. 10101a (reprinted in App., *infra*, 1a-2a). The first two elements of the transportation policy (49 U.S.C. 10101a) are:

> (1) to allow, to the maximum extent possible, competition and the demand for services to establish reasonable rates for transportation by rail;
>
> (2) to minimize the need for Federal regulatory control over the rail transportation system.

An "important cornerstone" of the Staggers Act (H.R. Rep. 96-1035, 96th Cong., 2d Sess. 79 (1980)) was a substantial expansion of the Commission's exemption authority. The Commission is now directed to grant an exemption whenever it finds that further regulation is not necessary to carry out the National Rail Transportation Policy and either that the transportation or services involved are of "limited scope" or that further regulation is "not needed to protect shippers from the abuse of market power." 49 U.S.C. 10505(a)(2).[1] The Commission is instructed to revoke an exemption in whole or in part if it later concludes that regulation is necessary (49 U.S.C. 10505(d)). Significantly, Congress eliminated the requirement that exemption and revocation decisions must be preceded by notice to interested parties and an opportunity for a hearing. 49 U.S.C. 10505

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[1] The authority is limited in several additional respects not relevant here. See 49 U.S.C. 10505(e) and (g).

(b) and (d); H.R. Conf. Rep. 96-1430, *supra*, at 104-105.

In addition to the exemption in this case, the Commission has used its authority under Section 10505 to exempt from regulation the rail transportation of various commodities (*e.g.*, fresh fruits and vegetables, liquid iron chloride, frozen foods, and coal for export). It has also exempted all transportation provided in "piggyback" equipment (trailers and containers on flatcars), and has exempted all rail transportation from certain requirements of 49 U.S.C. 10726 (long and short haul provisions).

2. The Commission's Decision

On consideration of comments filed by more than 200 parties, including four federal departments, the Commission (over the dissent of Chairman Taylor) issued a decision (Pet. App. 103a-152a) exempting railway boxcar traffic (other than carriage of nonferrous recyclable materials) from major regulatory restrictions under the Interstate Commerce Act.[2] The decision may conveniently be divided into three parts: (1) exemption of boxcar traffic from maximum rate regulation, (2) exemption of boxcar traffic from regulatory provisions restricting a carrier's right to withdraw from or to change a joint rate agreement, and (3) partial exemption of railroads from regulations setting the terms of rentals of boxcars owned or leased by one carrier while they are under the control of another. The Commission also removed all antitrust immunity from the exempted activities. The Commission granted the exemption on the statutory ground that "continued regulation is

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[2] Although not required under the Act to do so, the Commission published a notice of proposed rulemaking, 47 Fed. Reg. 4100 (1982), and invited, received, and considered comments from interested parties. See Pet. App. 108a-111a.

not necessary either to carry out the rail transportation policy of section 10101a or to protect shippers from the abuse of market power" (Pet. App. 112a).

a. With respect to maximum rate regulation, the Commission determined that continued regulation is not necessary to carry out the statutory policy (49 U.S.C. 10101a(6)) of maintaining reasonable rates in the absence of effective competition. The Commission reasoned that truck competition for the transportation of commodities ordinarily transported by boxcar is "pervasive and limits the railroads' pricing freedom" (Pet. App. 113a). Unlike other forms of railway transportation, where there is no convenient trucking alternative, boxcars face intense competition from trucks across their full line of service. "Virtually anything that can be transported in a boxcar can be transported in a truck," and since truck transport "tends to be faster, more accessible, more convenient, and sometimes less damaging to freight than rail service," railroads can compete for boxcar commodities only by offering a better price. *Ibid.* In addition, there are constraints deriving from other forms of transportation, product competition, geographic competition, and "leverage" exercised by "powerful shippers" (*id.* at 113a-114a). "Thus, the market itself places an effective ceiling on rail rates for boxcar transportation, and regulation is unnecessary to assure that boxcar rates do not rise to unreasonably high levels" (*id.* at 113a).

b. Several parties before the Commission questioned the application of this boxcar exemption to joint rates, which are regulated under 49 U.S.C. 10705. The Commission found, however, that the competitive character of transportation of boxcar commodities leads to the same conclusion for joint as for single-line rates. It therefore concluded that continued regulation of joint rates was not necessary to

carry out the statutory policies of developing and continuing a sound rail transportation system (49 U.S.A. 10101a(4)) or providing effective coordination among railroads (49 U.S.C. 10101a(5)). See Pet. App. 123a.

The Commission reasoned that efficient joint rates would be preserved because, "[i]n the face of truck competition, carriers have strong incentives to make through rail service as attractive as possible" (Pet. App. 123a). Participating carriers would neither cancel efficient joint rates nor "insist on a division of profits so disproportionate as to force the other to withdraw from the movement" (*id.* at 124a).

On petition for reconsideration, the Commission further explained (Pet. App. 161a) that joint rates could be cancelled even under regulation; the effect of the exemption was therefore to avoid the "unnecessarily expensive and time consuming" manner of resolving disputes under the prior system. Moreover, there exist other means of handling through traffic efficiently "even in the absence of joint rates" (*ibid.*). Most importantly, the Commission reiterated that "where joint rates enhance the attractiveness of through rail service, we expect that they will continue to be offered even in the absence of regulation" because both small and major carriers "benefit from the revenue earned on this traffic" (*ibid.*). The need to compete with trucks will induce railroads to use the most efficient routes available, whether joint or single-line. "Carriers cannot afford the luxury of preserving inefficient routes when competitive pressures force them to reduce costs as much as possible" (*id.* at 162a (footnote omitted)). See also Pet. App. 199a-200a.

c. The third major part of the Commission's decision was its partial exemption of boxcars from the prior scheme of mandatory rental charges for roll-

ing stock owned by one railroad while it is on the lines of another. Under these rules the "originating" carrier—the boxcar owner or lessee—had the right to charge the "terminating" or "destination" carrier—the railroad with control over the boxcar—a rental fee (called a "per diem"), up to a maximum rate set by the Commission, even when the car stood idle on the terminating carrier's tracks. Moreover, the originating carrier could demand the return of its car at the terminating carrier's expense. The terminating carrier was obliged to pay these fees, if demanded by the originating carrier, and was prohibited from imposing fees for the costs of storage or of returning the cars. Pet. App. 163a-164a.

The Commission found that these car hire rules had two deleterious consequences. First, they created an incentive for "unnecessary cross hauling of empty cars" (Pet. App. 163a). Since railroads receive rental fees when their own cars are on the tracks of another railroad, they will tend to load their own cars with cargo and return the cars of other lines empty. This unnecessary criss-crossing of empty boxcars inflates operating costs. See (*ibid.*). Second, the per diem rates "create[d] at least the illusion of a guaranteed return on investment," thus "encouraging investors to acquire cars without regard to the adequacy of the existing fleet." *Id.* at 164a. See also Pet. App. 127a-128a.

The Commission's solution was to exempt all negotiated agreements from the car hire regulations and to create an incentive to reach agreements by permitting terminating carriers to offset storage fees on empty boxcars stored for more than three days against the per diems up to the per diem rate and

to charge up to the variable cost of returning empty boxcars upon request (35 cents per mile).[3]

The Commission concluded that the exemption of boxcars from rate regulation (both joint and single rate) and the partial exemption from car hire rules would benefit the public by providing improved transportation service, lower overall rate levels, and better car use. Pet. App. 138a. The Commission emphasized, however, that it would stand ready to revoke the exemption, in whole or in part, if experience showed that reregulation was necessary (*ibid.*):

> The public should be apprised that we have every intention of reviewing this matter, and we wish to leave no doubt that we will correct problems should they develop as we gain experience under this exemption.

3. The Court Of Appeals' Decision

The court of appeals sustained the Commission's decision to exempt boxcar traffic from maximum rate regulation insofar as it pertained to transportation not involving joint rates. The court affirmed the Commission's "finding that rail carriers did not have monopoly power in the market for transport of commodities shipped by boxcars" (Pet. App. 33a). The

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[3] In its initial decision, the Commission commented that its partial exemption from the car hire rules "could be construed in some respects as being new regulation" (Pet. App. 136a). "To allay any doubts" regarding its statutory authority, therefore, the Commission relied on its regulatory authority under 49 U.S.C. 11122 as well as its exemption authority under 49 U.S.C. 10505 (Pet. App. 136a). In its opinion on denial of petitions for reconsideration, the Commission, for procedural reasons, "withdr[e]w any reliance on section 11122 as authority" for its decision (*id.* at 167a), noting that the action was in fact a "partial exemption from regulation subject to conditions" (*ibid.* (footnote omitted)) and thus within its exemption authority.

court also approved "the Commission's position that its authority to revoke the exemption is an appropriate mechanism to correct any post-exemption market abuse" (*ibid.*).

However, the court overturned the exemption as it applied to joint rates.[4] In so doing, the court did not question the Commission's determination that continued regulation was not necessary to protect shippers from an abuse of market power (see 49 U.S.C. 10505(a)(2)(B)), but rested its decision on the conclusion that the Commission had inadequately considered the necessity of the regulation under the National Rail Transportation Policy, 49 U.S.C. 10101a. See Pet. App. 42a.

The court held (Pet. App. 42a) that the Commission failed "to adequately explain its crucial assertion that large long-haul carriers will not close off efficient routes of small short-haul carries." Moreover, the court found an "even more fundamental problem" with the Commission's analysis—its "assumption that the [National Rail Transportation] policy is satisfied as long as efficient routes are not cancelled or forced out of service." *Id.* at 44a. Specifically, the court stated (*id.* at 45a) that the Commission "totally ignored the division of profits" between large long-haul and small short-haul carriers.

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[4] Since an estimated 70% of all rail traffic moves over routes subject to joint rates (see H.R. Rep. 96-1035, *supra*, at 41), the portion of the court's decision that upheld the Commission's exemption will affect but a small part of the industry. The court acknowledged (Pet. App. 92a) that deregulating single line transportation but not joint rate transportation could cause a "disequilibrium" in the transportation market, because it might induce shippers to shift from the regulated to the unregulated sector, or vice versa, or create "other dislocations in the boxcar freight market."

The court of appeals also invalidated the Commission's partial exemption from the car hire rules, on the rationale that the partial exemption was in fact "regulation" rather than "deregulation," and thus not authorized under Section 10505. Pet. App. 60a-69a. This is because, "[i]n allowing storage charges and return fees the Commission, rather than merely deregulating, has altered the relative bargaining positions of the carriers and has influenced the allocation of the benefits that will flow from the cost savings associated with decreasing market inefficiencies" (*id.* at 60a).[5]

ARGUMENT

In passing the Staggers Rail Act of 1980, Congress formally concluded that "most transportation within the United States is competitive" and that "many of the Government regulations affecting railroads have become unnecessary and inefficient." § 2(3) and (4), 49 U.S.C. 10101a note. Although Congress itself was not able to identify every application of regulations that is now unnecessary and inefficient, it entrusted the Commission with the power to do so by "actively pursuing exemptions." H.R. Rep. 96-1035, 96th Cong., 2d Sess. 60 (1980); H.R. Conf. Rep. 96-1430, 96th Cong., 2d Sess. 105 (1980). Congress intended that, through its exemption power, the Commission would remove "as many as possible of the Commission's restrictions on charges in prices and services by carriers" and urged the Commission to "adopt a policy of reviewing carrier actions after the fact to

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[5] The court of appeals also rejected the Commission's application of the boxcar exemption to the Alaska Railroad (Pet. App. 69a-83a); the Commission has not petitioned for review of that portion of the judgment. The court upheld the Commission's decision against specific challenges by Canadian railroads and the Port of Oakland (*id.* at 83a-91a).

correct abuses of market power" (*ibid.*). Exercise of the exemption authority is therefore intended to be "experimental" and "innovative" (H.R. Rep. 94-725, 94th Cong., 1st Sess. 243 (1975)). Indeed, to free the Commission from administrative constraints and enable it to act quickly and flexibly, Congress even took the extraordinary step of allowing the Commission to impose or to revoke exemptions without giving notice or an opportunity for a hearing.

The Commission's decisions in this case and in its *Railroad Exemption—Export Coal*, 367 I.C.C. 570 (1983), vacated and remanded, 745 F.2d 76 (D.C. Cir. 1984), petition for cert. pending, No. 84-884, are two examples of the Commission's aggressive use of its exemption authority, in precisely the active and experimental manner Congress intended. In both instances, the District of Columbia Circuit has invalidated the Commission's exemption decision without disturbing the agency's findings that competitive factors would generally inhibit abuses of market power by the newly deregulated railroads, and that any abuses that might occur could be remedied by carefully-tailored revocations. Both court decisions were based on the concern that in some instances the division of profits from the activities in question might not be "fair." In the *Export Coal* case, the question is whether *shippers* might receive less than their fair share of the "rents" derived from the movement of coal for export; the basis for the court's decision was the importation of regulatory policies from other sections of the Act into the concept of "abuse of market power" under 49 U.S.C. 10505 and a criticism of the Commission's balance of the competing policies within

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[6] See Brief for the United States, *ICC* v. *Coal Exporters Ass'n*, No. 84-884. A copy of that brief will be provided to the parties in this case.

the National Rail Transportation Policy, 49 U.S.C. 10101a.[6] In this case, the question is whether smaller *carriers* might receive less than their fair share of the "rents" derived from the movement of cargo on through routes; the basis for the court's decision was the importation of policies found in the legislative history of 49 U.S.C. 10705a into the National Rail Transportation Policy and the court's own independent assessment of the content and relative importance of parts of that Policy.

The consequence of the decision below, especially in light of the similar decision in the *Export Coal* case, is to frustrate the Commission's ability to comply with its deregulatory mandate under the Staggers Act. Rather than being able to exempt broad categories of rail transportation service from regulation on the basis of a reasoned assessment of competitive factors, and to protect against possible abuses through the revocation authority, as Congress intended, the holdings in these decisions will require the Commission to guarantee, in advance, that shippers and smaller carriers will continue to receive a "fair" level of revenues that in many cases might be in excess of that set by the market. Any other outcome, according to the court below, would "[c]ertainly" (Pet. App. 48a) or "self-evident[ly]" (*id.* at 45a) be in violation of the National Rail Transportation Policy.

Although generally phrased in terms of requiring the Commission to "consider" a relevant, but overlooked factor, the decision below in fact engrafts an additional substantive requirement on the Commission's exemption authority. Fidelity to the Court's interpretation of the National Rail Transportation Policy might well preclude the Commission from issuing a broad exemption where it cannot guarantee

that the division of rents after deregulation will not be adverse to smaller carriers.[7]

The decision below conflicts with the only other court of appeals decision dealing with the exemption of a type of transportation service ("piggyback" transportation), and with general principles established by this Court for judicial review of policy decisions by the Commission pursuant to explicit delegation of authority. But even in the absence of a conflict, the decision below would warrant review because any exercise by the Commission of its exemption authority is reviewable in the District of Columbia. 28 U.S.C. 2343. As a practical matter, the Commission will be compelled to conform its future exemption decisions to the court's holding. The result will be to eviscerate "an important cornerstone" of the congressional effort to decrease unnecessary and inefficient regulation of the railroad industry.[8]

1. Joint Rates

There are two statutory prerequisites to the Commission's exercise of its exemption authority. The Commission must find, first, that continued regulation "is not necessary to carry out the transportation policy" of the Act. This refers specifically to the 15 elements listed in 49 U.S.C. 10101a. The Commis-

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[7] As if to underscore that its decision is substantive, and not merely procedural, in character, the court warned the Commission that subsequent rules "of course must avoid the problems we have identified in this opinion of large carriers abusing their power over small carrier co-participants in through routes" (Pet. App. 93a, citing *ILGWU* v. *Donovan*, 733 F.2d 920 (D.C. Cir. 1984) (in which the agency, on remand and after consideration of the relevant factors identified by the court, reinstated a limited version of its former rule on a temporary basis, and was reversed by the court for so doing)).

[8] If the petition is granted, the United States and the Commission undertake to file a joint brief on the merits.

sion must find, second, that continued regulation is "of limited scope" or "is not needed to protect shippers from the abuse of market power." 49 U.S.C. 10505(a). The second test was concededly satisfied in this case (Pet. App. 33a-34a) and, accordingly, the court of appeals' decision was based entirely on the determination that continued regulation of joint rate agreements involving boxcar traffic may be necessary to carry out the National Rail Transportation Policy.

The Commission found that, as a result of competition from the trucking industry, the railroads have lost much of the traffic that has historically been moved by boxcar, and that "[t]his trend will not be arrested unless the railroads can enhance the attractiveness of boxcar service through cost reduction and more flexible pricing" (Pet. App. 156a). Relying heavily on its experience with previous exemptions, especially the exemption for "piggyback" service, in which "declines in railroad traffic were dramatically reversed with the cessation of regulation" (*id.* at 182a), the Commission predicted that the exemption here would enable the railroads to attract traffic back to boxcars, to the benefit of both large and small carriers as well as the public (*id.* at 162a). The Commission thus concluded (*id.* at 126a) that the exemption

> will actively promote the objectives of the rail transportation policy in a number of ways. Clearly, it will: (1) allow competition and the demand for services to establish reasonable rates (section 10101a(1)); (2) minimize the need for Federal regulatory control over a substantial portion of the rail transportation system (section 10101a(2)); (3) promote more efficient pricing and service on boxcar traffic and allow carriers, to the extent possible, to earn adequate revenues on this traffic, by removing procedural

regulatory burdens and allowing rail management to respond flexibly to market conditions (section 10101a(3)); (4) promote effective competition with motor carriers (sections 10101a(4) and (5)); (5) encourage efficient railroad management and elimination of noncompensatory rates by allowing full flexibility to manage boxcar service in the most economic manner (section 10101a(10); and finally, (6) to the extent that it enables railroads to retrieve business lost to the motor carrier industry, promote energy conservation (section 10101a(15)).

The court of appeals did not address, or even allude to, these findings regarding the National Rail Transportation Policy, and they may therefore be assumed to stand.

The court, however, found fault with the Commission's conclusion that continued regulation is not necessary to carry out the transportation policy because the Commission gave inadequate attention to the "division of profits [between large and small carriers] likely to result * * * in the absence of regulation" (Pet. App. 45a).[9] It reached this conclusion

[9] The court also found that the Commission had failed adequately to explain "its crucial assertion that large long-haul carriers will not close off efficient routes of small short-haul carriers" (Pet. App. 42a). However, the Commission's extensive discussions of this question (see *id.* at 123a-124a, 161a-162a, 199a-200a) are based on the same rationale that, as the court agreed, justified the exemption of single-line rates from regulation. The rationale is that competitive pressure from trucks and other sources is so intense that rail carriers must, in order to compete effectively for boxcar traffic, use the most efficient routes possible. Accord, *Central Vermont Ry.* v. *ICC*, 711 F.2d 331, 335 (D.C. Cir. 1983); *Chesapeake & O. Ry.* v. *United States*, 704 F.2d 373, 377 (7th Cir. 1983) (in an unregulated market "it would be commercial suicide" for long-haul carrier to close efficient through routes over the lines of other carriers). Elsewhere in its opinion, the court seemingly

on the basis of its own independent analysis of the statutory policy.

The court focused on three of the 15 elements of the National Rail Transportation Policy. First, the court invoked the statutory policy of encouraging "the development and continuation of a sound transportation system with effective competition among rail carriers" (49 U.S.C. 10101a(4)), interpreting this policy as reflecting "Congress' unquestionable concern that large carriers might unfairly squeeze profits from captive small carriers" (Pet. App. 47a). Second, the court cited the policy of safeguarding against "predatory pricing and practices * * * and * * * unlawful discrimination." 49 U.S.C. 10101a (13); see Pet. App. 48a. The boxcar exemption would violate this policy, according to the court, because it "[c]ertainly" is "unfair competition" for a larger carrier to use its "monopoly power" to "appropriate a captive short-haul carrier's joint rate profits that derive from the smaller carrier's efficiency" (*ibid.*). Third, the court looked to the policy of encouraging the "elimination of noncompensatory rates for rail transportation." 49 U.S.C. 10101a (10); see Pet. App. 48a The court inferred, as a negative implication, that this policy prevents "monopoly carriers from charging rates that produce an unreasonable return for their costs" (*id.* at 49a).

The court thus found that "a fair division of joint rates [is] an important means of carrying out the rail transportation policy" (Pet. App. 50a), and made

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acknowledged that the Commission had fully addressed this point. See, especially, Pet. App. 39a-41a, 45a, 46a; see also *id.* at 63a ("if there are inefficiencies creating unnecessary costs, the parties, inspired by the lure of larger profits, will negotiate to save these costs regardless of their initial bargaining positions").

clear that such a "fair" division might require more than a compensatory return in some cases (*id.* at 46a, 48a). Accordingly, the court invalidated the boxcar exemption, as it applies to joint rates, because of the Commission's purported "total failure to consider the effect of joint rate exemption on this division" (*id.* at 50a).

There are three serious errors in the court's decision.

a. Most important to the Commission's continued ability to employ its Staggers Act exemption authority in the manner Congress intended is that the court of appeals injected an additional, and troublesome, element in the National Rail Transportation Policy that was not enacted or intended by Congress—that is, ensuring the "fair division" of profits between large long-haul and small short-haul carriers. The court's labored interpretations of 49 U.S.C. 10101a(4), (10) and (13) (see Pet. App. 45a-49a) amply make the point. The policies cited by the court are designed to promote "competition among rail carriers" (49 U.S.C. 10101a(4))—not, as the court would have it, to protect smaller carriers from the consequences of competition; to prevent "predatory pricing" and "unlawful discrimination" where the antitrust laws are inadequate to do so (49 U.S.C. 10101a(13))—not, as the court would have it, to prevent hard bargaining over various compensatory levels of return; and to eliminate "noncompensatory rates for rail transportation" (49 U.S.C. 10101a(10))—not, as the court would have it, to preclude rail carriers from earning more than a compensatory return in a competitive market. Certainly, none of these policies expressly, or by necessary implication, requires the Commission to shield smaller carriers from competition where, as the Commission found, efficient through routes and

joint rates would be preserved. See *Chesapeake & O. Ry.* v. *United States*, 704 F.2d 373, 376 (7th Cir. 1983).

There is no established policy that the Commission has an obligation to oversee the "fairness" of divisions of revenues from joint rates, under Section 10705 or elsewhere. The general rule is that, although the Commission has authority to establish "reasonable" divisions of joint rates (49 U.S.C. 10705(a)(1)), divisions are normally a "private matter" between the connecting carriers. *Pennsylvania* v. *ICC*, 561 F.2d 278, 282 (D.C. Cir. 1977), cert. denied, 434 U.S. 1011 (1978); see *St. Louis S.W. Ry.* v. *United States*, 245 U.S. 136, 139 n.2 (1917); *Trailer Marine Transport Corp.* v. *FMC*, 602 F.2d 379, 382 n.8 (D.C. Cir. 1979). Thus, even assuming that the court of appeals is correct that in exempting boxcar traffic from the joint rate regulations of Section 10705 the Commission had to "consider why Congress adopted the provision in the first place" (Pet. App. 41a), it would not follow that it had to consider whether resultant divisions would be "fair."

The court of appeals' free-ranging interpretation of the National Rail Transportation Policy was based, in large part, on comments by members of the House of Representatives (quoted at Pet. App. 45a-47a) during debate on another section of the Staggers Act, now 49 U.S.C. 10705a. This Section permits carriers to cancel (or to impose surcharges on) noncompensatory joint rates, without Commission approval, with certain narrow exceptions. Since joint rate cancellations under Section 10705a would be permitted unilaterally, without Commission approval, and since they would be permitted even where the railroads have significant market power, members of Congress understandably were concerned about protection for

shippers and small carriers. The court erred, however, in treating these statements as authoritative guides to the National Rail Transportation Policy, to which they do not pertain. The quoted statements do not express any congressional judgment concerning *competitive* transportation services, as are involved here, where market forces constrain the ability of a carrier to exploit its position. Nor do they apply to exemptions under Section 10505, where shippers and carriers are protected by the Commission's continuing revocation power.

Significantly, the small carrier protective provisions of 49 U.S.C. 10705a discussed in the quoted legislative history do not apply to joint rate cancellations under 49 U.S.C. 10705(e). *Southern Ry.* v. *ICC*, 681 F.2d 29 (D.C. Cir. 1982). The Commission is free to approve joint rate cancellations, in the public interest, without addressing these provisions. It is curious for the court to hold that the policies reflected by those provisions are impliedly incorporated in the National Rail Transportation Policy, when they are not even incorporated in the companion section, 49 U.S.C. 10705(e).

One of the comments quoted by the court, by Representative Lee, indicates his hope that the "exemption clause"—presumably 49 U.S.C. 10505—would not be "used to 'end run' the joint rate provisions" of Section 10705a. However, nothing in the language or legislative history of the exemption provision suggests that any different standard was intended to apply to joint rate exemptions. Indeed, both Representative Madigan and Representative Staggers stated that the conferees "fully expect" the Commission to use its exemption authority to abolish joint rate requirements. 126 Cong. Rec. 28430 (1980); *id.* at 28431-28432.

Congress quite specifically set forth in 49 U.S.C. 10505, and by reference in 49 U.S.C. 10101a, the

standards it intended the Commission to apply in determining whether to grant an exemption. Those standards include explicit protections for *shippers* from an abuse of market power, but contain no such protection for competitive *carriers*. In requiring the Commission to conduct a painstaking analysis of the "division" of profits, over and above a compensatory return, between large and small carriers, the court of appeals has read into the National Rail Transportation Policy an element of its own making, and has elevated that element to a prominence that is wholly unwarranted.

b. But even assuming that the division of profits among carriers is a necessary element in transportation policy, it is evident that the Commission considered the issue; the court has supplied no reason, other than its own contrary opinion, for concluding that the Commission's judgment is arbitrary and capricious. The Commission found—and the court affirmed in another context (Pet. App. 32a-33a)—that railroad boxcar transportation faces stiff competition from trucks and other sources for virtually every commodity. Given that competition, the railroads have a strong incentive to reduce costs in every way possible, including using the most efficient routes. Accordingly, "it is unlikely that a carrier acting in an economically rational manner would close efficient routings," as the Commission stated (*id.* at 124a). Moreover, the Commission found that "[i]n reaching agreement on divisions on joint rates, neither carrier will insist on a division of profits so disproportionate as to force the other to withdraw from the movement to avoid a loss and thus to forfeit the traffic for both carriers" (*ibid.*). Large long-haul railroads "can not afford to undermine the health of the [small] carriers that supply them with an essential flow [of] traffic" (*id.* at

198a); "the penalty for a large connecting carrier that fails to allow the small carrier its required revenue is loss of this traffic and loss of a contribution toward its own capital cost" (*ibid.*).[10]

Far from being arbitrary or capricious, this conclusion is a sound economic judgment; a similar conclusion has been reached, in other contexts, by other panels and other courts. See *Detroit, T. & I.R.R.* v. *United States*, 725 F.2d 47, 50 (6th Cir. 1984); *Central Vermont Ry.* v. *ICC*, 711 F.2d 331, 335 (D.C. Cir. 1983); *Chesapeake & O. Ry.* v. *United States*, 704 F.2d at 377.[11] The court of appeals' holding that

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[10] We are thus baffled by the court's repeated assertions that the Commission "totally disregarded," "total[ly] fail[ed] to address," or "total[ly] fail[ed] to consider" the effect of the joint rate exemption on the division of revenues between long and short haul carriers (Pet. App. 47a, 48a, 50a). The quotations in text plainly show that the Commission did so. Moreover, the issue has been considered by the Commission in greater depth in other contexts. See *Traffic Protective Conditions*, 366 I.C.C. 112, 122-126 (1982), aff'd in relevant part, 725 F.2d 47 (6th Cir. 1984).

In any event, the parties before the Commission did not raise the issue of the division of revenues, and nothing in the National Rail Transportation Policy explicitly addresses the question. The Commission could hardly be faulted for failing to give more attention to an issue that was not raised by the parties and is not part of its statutory standards.

[11] As the Commission pointed out (Pet. App. 174a-175a), small carriers have significant bargaining power in their dealings with larger carriers. Absent regulatory constraints or unusually high transaction costs, the only instances in which a long-haul carrier is able profitably to "squeeze" a more efficient short-haul carrier is when it has a route that is nearly as efficient as the short-haul carrier's route. *Traffic Protective Conditions*, 366 I.C.C. 112, 126 (1982), aff'd in relevant part, 725 F.2d 47 (6th Cir. 1984); see generally Carlton & Klamer, *The Need for Coordination Among Firms, With Special Reference to Network Industries*, 50 U. Chi. L. Rev. 446, 452-453

this analysis is legally insufficient suggests a virtually insuperable barrier to exercise of the exemption authority. Congress did not expect that the Commission could guarantee, in advance, that an exemption would have its desired effects. "A decision to deregulate by exemption some portion of railroad transportation necessarily cannot be made on the basis of data from past experience—no such data exists." *American Trucking Ass'ns* v. *ICC*, 656 F.2d 1115, 1127 (5th Cir. 1981). Deregulation is to be the norm, continued regulation of prices and services the exception. H.R. Conf. Rep. 96-1430, *supra*, at 105.

An oddity of the decision below is that the court's assumptions in this section of the opinion—that large carriers in fact possess "monopoly power" (Pet. App. 45a, 48a) such that they are able to obtain an "unreasonable" (*id.* at 49a), "disproportionate," (*id.* at 48a), or "exorbitant" (*ibid.*) return—are directly contrary to the court's explicit findings in Section II of its opinion that, with respect to boxcar traffic, "rail carriers d[o] not have monopoly power" (Pet. App. 33a) and thus lack the ability to extract unreasonable returns.[12] The Commission's conclusions regarding the competitive nature of boxcar transportation, affirmed by the court of appeals for one purpose, do not suddenly become arbitrary and capricious when applied to the joint rate issue.[13]

(1983). In such instances, the "squeeze" will perforce be relatively small, and the efficiency loss likewise. The Commission would be justified in determining that such a loss would be outweighed by the benefits of the exemption in the ordinary case. Cf. *Traffic Protective Conditions*, 366 I.C.C. at 126.

[12] Perhaps the inconsistency is explained by the fact that different parts of the opinion below were written by different judges (Pet. App. 15a n.*).

[13] The court attempted to elide analysis by relying on a passage in the Commission's opinion in which, according to the

c. Further, even assuming the court's nonliteral reading of the transportation policy were valid, and that the court's economic assumptions rather than the Commission's determinations were controlling, the court still would have erred in overturning the Commission's decision. The Commission explicitly determined that the exemption would promote some seven elements of the National Rail Transportation Policy. See pages 15-16, *supra*. The court of appeals did not take issue with those determinations. The most that could be said, therefore, is that in this instance the various elements of the transportation policy may conflict. But the task of weighing conflicting elements of the national transportation policy has been entrusted to the Commission, not to the court of appeals. *Schaffer Transportation Co.* v. *United States*, 355 U.S. 83, 92 (1957); *Erickson Transport Corp.* v. *ICC*, 728 F.2d 1057, 1066 (8th Cir. 1984); *Baggett Transportation Co.* v. *United States*, 666 F.2d 524, 530-531 (11th Cir. 1982); cf. *Chevron U.S.A. Inc.* v. *NRDC*, No. 82-1005 (June 25, 1984), slip op. 26-28. It is not the place of the reviewing court to decide, contrary to the Commission, that it is "self-evident" that the consequences of the Commission's decision "would not comport with the rail transportation policy" (Pet. App. 45a).

d. The approach taken by the court below conflicts sharply with that taken by the Fifth Circuit in reviewing the Commission's earlier exemption of rail transportation in "piggyback" cars (trailers and containers on flatcars) from regulation under the

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court (Pet. App. 44a), the Commission "apparently conceded that large long-haul carriers may have monopoly power over small short-haul carriers." However, the cited page in the Commission's opinion, Pet. App. 124a, contains no such concession, and the opinion expressly and repeatedly expresses the opposite conclusion.

Act. *American Trucking Ass'ns* v. *ICC*, 656 F.2d 1115 (1981). Analytically, the two exemptions are virtually identical; in both instances, the Commission determined that competition from motor carriers and other sources was sufficient to guard against any abuse of market power. See 656 F.2d at 1123. In both instances, the exemptions applied to joint rates as well as to single line rates; the arguments adopted by the court below would therefore have been fully available to the Fifth Circuit as well. However, the Fifth Circuit easily sustained the exemption in relevant part, applying a narrow standard of review and deferring to the congressional judgment that the exemption authority should be used vigorously and experimentally. *Id.* at 1127. The court noted that Congress intended the Commission to "exercis[e] its exemption authority in the face of uncertainty as to the effect of an exemption," and to " 'review[] carrier actions after the fact to correct abuses of market power.' " *Ibid.*, quoting H.R. Conf. Rep. 96-1430, *supra*, at 105. The court of appeals here accorded no weight whatsoever to this congressional policy, and instead imposed additional substantive standards of its own making that—had they been applied to the "piggyback" exemption—would have invalidated that exemption as well.

If not reviewed, the decision below will seriously impair the Commission's ability to employ the exemption power in the way Congress intended. Virtually every exemption from every railroad regulation will open the possibility that some shippers or small competing carriers will be placed in a less advantageous bargaining position than they were under regulation. This will necessarily affect the "division" of profits from rail transportation. Congress did not intend to allow such concerns to stand in the way of elimi-

nation of unnecessary and inefficient regulation, where the regulation is not needed to carry out the National Rail Transportation Policy as a whole. In light of the importance of the Staggers Act exemption authority to the congressional purpose of revitalizing the rail industry, the decision below warrants review.

2. Car Hire Rules

The court of appeals' invalidation of the partial exemption of boxcars from the car hire rules is in error, is of considerable practical importance, and should be reviewed along with the joint rate issue.[14]

The court did not question the Commission's conclusion that the car hire rules, in the present context, are unnecessary and inefficient. Indeed, the rules have generated major unnecessary operating costs by creating an incentive for expansion of boxcar fleets without regard to demand for boxcar services, and for cross hauling of empty boxcars rather than returning a boxcar to its originating carrier with cargo. A significant portion of the savings from the boxcar exemption is expected to derive from the car hire portion of the exemption.

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[14] If the Court decides not to review the joint rate issue, we do not recommend considering the car hire issue independently. The decision below appears to leave room for adoption of this regulation on remand under other authority (Pet. App. 65a). Moreover, the car hire rules are under consideration in a wider context in Ex Parte No. 334 (Sub-No. 5), *Zone of Reasonableness for Car Hire Charges*, 364 I.C.C. 299 (1980), and Ex Parte No. 346 (Sub-No. 19), *Boxcar Car Hire and Car Service—Advance Notice of Proposed Rulemaking*, 49 Fed. Reg. 27333 (July 3, 1984). While we are advised that neither of these proceedings is likely to render this case moot, they would offer the Commission alternative means for accomplishing its objectives in the event the petitions were denied.

The court of appeals, however, concluded that the Commission's action constituted "regulation" rather than "deregulation," and thus that it was beyond the agency's authority under 49 U.S.C. 10505. Pet. App. 60a-69a. The court reasoned that the Commission did not merely exempt terminating carriers from parts of the car hire rules, but instead "altered the relative bargaining positions of the carriers" and "influenced the allocation of the benefits that will flow from the cost savings associated with decreasing market inefficiencies" (Pet App. 60a).[15]

This is pure semantics. There can be no doubt that, had the Commission characterized its decision as exempting terminating carriers from the obligation to pay per diem charges, it would be considered "deregulation." Conversely, had the Commission characterized the decision as introducing a new, mandatory storage fee to be imposed at the option of the terminating carrier at a maximum level set by the Commission (equal to the per diem rate), this would appear to be "regulation." But the two decisions would have identical effects—and both are identical to the decision as actually set forth by the Commission. Similarly, while the imposition of a charge (subject to a 35 cents per mile limit) for returning an empty boxcar upon request might appear to be "regulation," it can as easily be said that exempting a terminating carrier from the rule prohibiting any charge for performing this service, upon the condition that no charge be imposed in excess of variable cost (35 cents per mile), is "deregulation." And of course, the third element of the car hire exemption—exemption of negotiated car hire agree-

[15] Of course, under the decision below, there will be no such "cost savings," since the market inefficiencies of the car hire rules will continue.

ments—would appear to be "deregulation" in any light.

It does not suffice to state, with the court of appeals, that the car hire exemption is "regulation" because it "shifted entitlements" among participants in the regulatory scheme rather than removing them (Pet. App. 61a). Were that the test, virtually all partial deregulation would be deemed "regulation" because the effect of a change in a regulatory scheme is almost always to shift entitlements among parties to the transaction.

The only sensible, non-circular test for "deregulation" is whether the result is what Congress intended—an increase in the degree to which market forces determine the deployment of resources. There can be no doubt that the partial car hire exemption moves in this direction. The exemption will allow the demand for boxcars to determine compensation levels (Pet. App. 132a, 181a) and will impose the costs of empty car movements on those who demand them (*id.* at 131a, 177a). Perhaps most important, it will create an incentive for the parties to enter into their own agreements. Even Chairman Taylor, in dissent, described the car hire decision as an "effort to graft a little 'free market' onto regulation" (*id.* at 145a).

The decision below conflicts with this Court's decisions in *ICC* v. *American Trucking Ass'ns*, No. 82-1643 (June 5, 1984), and *ICC* v. *Oregon Pacific Industries, Inc.*, 420 U.S. 184 (1975). In *American Trucking Ass'ns*, the Court held that the Commission has the authority to impose conditions on the approval of a proposed tariff, even where the effect of those conditions is to create an additional remedy not expressly provided by Congress. Slip op. 12-13. The same logic would apply to exemptions. The Commission characterized its car hire decision as "a partial

exemption from regulation subject to conditions" (Pet. App. 136a). It exempted terminating carriers from portions of the car hire rules, subject to the condition that they charge offsetting storage fees no greater than the per diem charges and return fees no greater than variable cost. Under the principle of *American Trucking Ass'ns*, that action is within the Commission's authority under 49 U.S.C. 10505. See also *Trans Alaska Pipeline Rate Cases*, 436 U.S. 631 (1978); *United States* v. *Chesapeake & O. Ry.*, 426 U.S. 500 (1976).

In *Oregon Pacific Industries*, the Court held that a change in demurrage charges for railway cars held at reconsignment points by terminating carriers for more than five days was a "suspen[sion]" of "rules, regulations, or practices then established with respect to car service," within the meaning of Section 1(15) of the Interstate Commerce Act, 49 U.S.C. (1976 ed.) 1(15). 420 U.S. at 186 (citation omitted). The Court did not indulge in semantical exercises with the term "suspension," such as were performed below with regard to the similar term "exemption"; rather, the Court upheld the Commission's decision on the ground that it was "not an unreasonable method" of achieving the congressional purposes. 420 U.S. at 191. Here, the Congress intended to replace regulation with "greater reliance on the marketplace" (§ 2(9), 49 U.S.C. 10101a note). The car hire exemption is "not an unreasonable method" of furthering that end.

CONCLUSION

The petitions for a writ of certiorari should be granted and the cases consolidated for argument.

Respectfully submitted.

REX E. LEE
Solicitor General

J. PAUL MCGRATH
Assistant Attorney General

LOUIS F. CLAIBORNE
Deputy Solicitor General

MICHAEL W. MCCONNELL
Assistant to the Solicitor General

JOHN J. POWERS, III
JOHN P. FONTE
Attorneys

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STATUTORY APPENDIX

1. 49 U.S.C. 10101a provides:

> In regulating the railroad industry, it is the policy of the United States Government—
>
> (1) to allow, to the maximum extent possible, competition and the demand for services to establish reasonable rates for transportation by rail;
>
> (2) to minimize the need for Federal regulatory control over the rail transportation system and to require fair and expeditious regulatory decisions when regulation is required;
>
> (3) to promote a safe and efficient rail transportation system by allowing rail carriers to earn adequate revenues, as determined by the Interstate Commerce Commission;
>
> (4) to ensure the development and continuation of a sound rail transportation system with effective competition among rail carriers and with other modes, to meet the needs of the public and the national defense;
>
> (5) to foster sound economic conditions in transportation and to ensure effective competition and coordination between rail carriers and other modes;
>
> (6) to maintain reasonable rates where there is an absence of effective competition and where rail rates provide revenues which exceed the amount necessary to maintain the rail system and to attract capital;
>
> (7) to reduce regulatory barriers to entry into and exit from the industry;

(8) to operate transportation facilities and equipment without detriment to the public health and safety;

(9) to cooperate with the States on transportation matters to assure that intrastate regulatory jurisdiction is exercised in accordance with the standards established in this subtitle;

(10) to encourage honest and efficient management of railroads and, in particular, the elimination of noncompensatory rates for rail transportation;

(11) to require rail carriers, to the maximum extent practicable, to rely on individual rate increases, and to limit the use of increases of general applicability;

(12) to encourage fair wages and safe and suitable working conditions in the railroad industry;

(13) to prohibit predatory pricing and practices, to avoid undue concentrations of market power and to prohibit unlawful discrimination;

(14) to ensure the availability of accurate cost information in regulatory proceedings, while minimizing the burden on rail carriers of developing and maintaining the capability of providing such information; and

(15) to encourage and promote energy conservation.

2. 49 U.S.C. 10505 provides:

(a) In a matter related to a rail carrier providing transportation subject to the jurisdiction of the Interstate Commerce Commission under this subchapter, the Commission shall exempt a

person, class of persons, or a transaction or service when the Commission finds that the application of a provision of this subtitle—

(1) is not necessary to carry out the transportation policy of section 10101a of this title; and

(2) either (A) the transportation or service is of limited scope, or (B) the application of a provision of this subtitle is not needed to protect shippers from the abuse of market power.

(b) The Commission may, where appropriate, begin a proceeding under this section on its own initiative or on application by the Secretary of Transportation or an interested party.

(c) The Commission may specify the period of time during which an exemption granted under this section is effective.

(d) The Commission may revoke an exemption, to the extent it specifies, when it finds that application of a provision of this subtitle to the person, class, or transportation is necessary to carry out the transportation policy of section 10101a of this title.

(e) No exemption order issued pursuant to this section shall operate to relieve any rail carrier from an obligation to provide contractual terms for liability and claims which are consistent with the provisions of section 11707 of this title. Nothing in this subsection or section 11707 of this title shall prevent rail carriers from offering alternative terms nor give the Commission the authority to require any specific level of rates or services based upon the provisions of section 11707 of this title.

(f) The Commission may exercise its authority under this section to exempt transportation that is provided by a rail carrier as a part of a continuous intermodal movement.

(g) The Commission may not exercise its authority under this section (1) to authorize intermodal ownership that is otherwise prohibited by this title, or (2) to relieve a carrier of its obligation to protect the interests of employees as required by this subtitle.

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